

DEPARTMENT OF STATE REVENUE

04-20170195R.ODR

**Final Order Denying Refund: 04-20170195R
Gross Retail and Use Tax
For the Years 2012 through 2015**

NOTICE: IC § 4-22-7-7 permits the publication of this document in the Indiana Register. The publication of this document provides the general public with information about the Indiana Department of Revenue's official position concerning a specific set of facts and issues. The "Holding" section of this document is provided for the convenience of the reader and is not part of the analysis contained in this Final Order Denying Refund.

HOLDING

Manufacturer of orthopedic implants was not entitled to a refund of use tax paid on surgical instruments Manufacturer provided without cost to hospitals and surgical facilities; the instruments were not prescribed or sold to the patients undergoing surgical procedures, and there was no evidence that the hospitals or surgical facilities rented or leased the instruments.

ISSUE

I. Gross Retail and Use Tax - Surgical Instruments.

Authority: IC § 6-2.5-1-2; IC § 6-2.5-2-1; IC § 6-2.5-2-1(a); IC § 6-2.5-2-1(b); IC § 6-2.5-3-1(a); IC § 6-2.5-3-2(a); IC § 6-2.5-4-1(b); IC § 6-2.5-4-10(a); IC § 6-2.5-5-18(a); IC § 6-2.5-5-18(c) (Effective July 1, 2015); *Rhoades v. Ind. Dep't of State Revenue*, 774 N.E.2d 1044 (Ind. Tax Ct. 2002); *Mynsberge v. Dep't of State Revenue*, 716 N.E.2d 629 (Ind. Tax Ct. 1999); *Tri-States Double Cola Bottling Co. v. Dep't of State Revenue*, 706 N.E.2d 282 (Ind. Tax Ct. 1999); *USAir, Inc. v. Ind. Dep't of State Revenue*, 623 N.E.2d 466 (Ind. Tax Ct. 1993); *General Motors Corp. v. Indiana Dept. of State Revenue*, 578 N.E.2d 399 (Ind. Tax Ct. 1991); *Indiana Dep't of State Rev. v. Kimball Int'l Inc.*, 520 N.E.2d 454 (Ind. Ct. App. 1988); *Indiana Dep't of State Revenue, Sales Tax Division v. RCA Corp.*, 310 N.E.2d 96 (Ind. Ct. App. 1974); [45 IAC 2.2-5-27](#); [45 IAC 2.2-4-27\(a\)](#); [45 IAC 2.2-5-27\(b\)](#); [45 IAC 2.2-5-28](#); [45 IAC 2.2-5-28\(g\)-\(h\)](#); [45 IAC 2.2-5-36](#); Revenue Ruling 2010-07ST.

Taxpayer argues that the Department erred when it denied it a refund of sales and/or use tax paid on the provision of various medical devices to hospitals and other surgical facilities.

STATEMENT OF FACTS

Taxpayer is in the business of manufacturing and distributing orthopedic implants, implant systems, and related products to for-profit hospitals, not-for-profit hospitals, and other surgical facilities. Taxpayer is headquartered in Indiana and operates manufacturing facilities throughout the United States and foreign locations.

Taxpayer filed a Claim for Refund (Form GA-110L) dated December 17, 2015. Taxpayer requested a refund of approximately \$560,000 in sales/use tax paid the state of Indiana during 2012, 2013, 2014, and 2015 on the ground that the surgical instruments were exempt from sales/use tax.

The Indiana Department of Revenue ("Department") conducted a review of the refund issuing a written report dated January 2017. The report noted that Taxpayer "remitted use tax to Indiana on . . . surgical instruments that it loaned out to [Taxpayer's] customers that were located in Indiana."

The Department concluded that Taxpayer was not entitled to the refund under the relevant Indiana exemption statute because Taxpayer neither sold nor rented the surgical instruments to the hospitals and surgical facilities and because the instruments were not prescribed to patients undergoing surgical procedures.

Taxpayer disagreed with the Department's decision and submitted a protest to that effect. This Final Order Denying Refund results.

I. Gross Retail and Use Tax - Surgical Instruments.

DISCUSSION

The issue is whether Taxpayer's medical instruments are exempt from Indiana's sales/use tax on the ground that

the instruments are properly categorized as exempt "durable medical equipment" under IC § 6-2.5-5-18(a).

Indiana imposes an excise tax called "the state gross retail tax" (or "sales tax") on retail transactions made in Indiana. IC § 6-2.5-2-1(a). A person who acquires property in a retail transaction (a "retail purchaser") is liable for the sales tax on the transaction. IC § 6-2.5-2-1(b).

Indiana also imposes a complementary excise tax called "the use tax" on "the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction." IC § 6-2.5-3-2(a). Use means the "exercise of any right or power of ownership over tangible personal property." IC § 6-2.5-3-1(a). The use tax is functionally equivalent to the sales tax. See *Rhoades v. Ind. Dep't of State Revenue*, 774 N.E.2d 1044, 1047 (Ind. Tax Ct. 2002).

By complementing the sales tax, the use tax ensures that non-exempt retail transactions (particularly out-of-state retail transactions) that escape sales tax liability are nevertheless taxed. *Rhoades*, 774 N.E.2d at 1047; *USAir, Inc. v. Ind. Dep't of State Revenue*, 623 N.E.2d 466, 468-69 (Ind. Tax Ct. 1993). The use tax ensures that, after such goods arrive in Indiana, the retail purchasers of the goods bear their fair share of the tax burden. To trigger imposition of Indiana's use tax, tangible personal property must (as a threshold matter) be acquired in a retail transaction. *Rhoades*, 774 N.E.2d at 1048. A taxable retail transaction occurs when; (1) a party acquires tangible personal property as part of its ordinary business for the purpose of reselling the property; (2) that property is then exchanged between parties for consideration; and (3) the property is used in Indiana. See IC § 6-2.5-1-2; IC § 6-2.5-4-1(b), (c); IC § 6-2.5-3-2(a).

The presumption in Indiana is that all retail sales are subject to sales tax unless expressly exempted by statute. IC § 6-2.5-2-1 ("An excise tax, known as the state gross retail tax, is imposed on retail transactions made in Indiana . . . except as otherwise provided in this chapter . . .").

In applying any tax exemption such as that relied upon by Taxpayer, the rule is that "tax exemptions are strictly construed in favor of taxation and against the exemption." *Indiana Dept. of State Rev. v. Kimball Int'l Inc.*, 520 N.E.2d 454, 456 (Ind. Ct. App. 1988). A statute which provides a tax exemption, however is interpreted against the taxpayer and in favor of the tax. *Indiana Dept of State Revenue, Sales Tax Division v. RCA Corp.*, 310 N.E.2d 96, 97 (Ind. Ct. App. 1974). "[W]here such an exemption is claimed, the party claiming the same must show a case, by sufficient evidence, which is clearly within the exact letter of the law." *Id.* at 100-101.

IC § 6-2.5-5-18(a) like all tax exemption provisions, is strictly construed against exemption from the tax. *Tri-States Double Cola Bottling Co. v. Dep't of State Revenue*, 706 N.E.2d 282, 283 (Ind. Tax Ct. 1999); *Mynsberge v. Dep't of State Revenue*, 716 N.E.2d 629, 636 (Ind. Tax Ct. 1999). Nevertheless, the Department is well aware of the countervailing rule that a "statute must not be construed so narrowly that it does not give effect to legislative intent because the intent of the legislature embodied in a statute constitutes the law." *General Motors Corp. v. Indiana Dept. of State Revenue*, 578 N.E.2d 399, 404 (Ind. Tax Ct. 1991).

The statute on which Taxpayer relies, IC § 6-2.5-5-18(a), provides as follows:

Sales of durable medical equipment, prosthetic devices, artificial limbs, orthopedic devices, dental prosthetic devices, eyeglasses, contact lenses, and other medical supplies and devices are exempt from the state gross retail tax, if *the sales are prescribed* by a person licensed to issue the prescription. (*Emphasis added*).

IC § 6-2.5-5-18 was amended effective July 1, 2015. The relevant portion of the statute states:

Transactions involving the following are exempt from the state gross retail tax if the end user acquires the property upon a prescription or drug order . . . that is required by the law for the transaction from a licensed practitioner:

- (1) Durable medical equipment (including a repair or replacement part).
- (2) Mobility enhancing equipment (including a repair or replacement part).
- (3) Prosthetic devices, including artificial limbs, orthopedic devices, dental prosthetic devices, eyeglasses, and contact lens (and including a repair or a replacement part;
- (4) Other medical supplies or devices that are used exclusively for medical treatment of a medically diagnosed condition, including a medically diagnosed condition due to:
 - (A) injury
 - (B) bodily dysfunction; or
 - (C) batteries; or

(D) accessories;

IC § 6-2.5-5-18(c).

Therefore, sales of "durable medical equipment" and supplies may be exempt if the equipment is "prescribed" to the purchaser. The Department's regulation, [45 IAC 2.2-5-27](#), explains:

- (a) The term "person licensed to issue a prescription" shall include only those persons licensed or registered to fit and/or dispense such devices.
- (b) Definition: The term "prescribed" shall mean the issuance by a person described in paragraph 1 of this regulation [*subsection (a) of this section*] of a certification in writing that the use of the medical equipment supplies and devices is necessary *to the purchaser* in order to correct or to *alleviate a condition brought about by injury to, malfunction of, or removal of a portion of the purchaser's body.* (*Emphasis added*).

Under IC § 6-2.5-5-18(a) and [45 IAC 2.2-5-27](#), a person having a "condition brought about by injury, malfunction of, or removal of a portion of the purchaser's body," may be eligible for a sales tax exemption if the "person" receives a proper prescription for the "medical equipment supplies and devices."

The Department's regulation [45 IAC 2.2-5-28](#)(g)-(h) repeats the qualification necessary to qualify for the exemption:

- (g) The sale to the user of medical equipment, supplies, or devices prescribed by one licensed to issue such a prescription are exempt from sales and use tax.
- (h) The term "medical equipment, supplies or devices", as used in this paragraph, are those items, the use of which is directly required to correct or alleviate injury to malfunction of, or removal of a portion of the purchaser's body.

Under IC § 6-2.5-5-18(a) and [45 IAC 2.2-5-28](#), sales of prescribed "medical equipment, supplies, or devices" are exempt if they are necessary to "correct or alleviate injury to, malfunction of, or removal of a portion of the purchaser's body." (*Emphasis added*).

Thus Taxpayer's protest, in effect, reiterates a line of argumentation that the Department has already specifically ruled on. Taxpayer's protest repeats the same lines of argument that it unsuccessfully made in its previous Revenue Ruling request. This Order Denying Refund incorporates the analysis and rationale of Revenue Ruling 2010-07ST in concluding that the surgical instruments are not prescribed to the patients undergoing the surgical procedures and that patients are not the purchasers of those instruments.

In Revenue Ruling 2010-07ST, the Department stated:

In support of its request, Taxpayer argues, *inter alia*, that its transactions involving orthopedic implants and related products, which Taxpayer concludes qualify as "durable medical equipment," are exempt from Indiana sales and use tax pursuant to [IC 6-2.5-5-18](#)(a) and [IC 6-2.5-3-4](#)(a). In the alternative, Taxpayer argues, *inter alia*, that its transactions involving orthopedic implants and related products are exempt from Indiana sales and use tax pursuant to [IC 6-2.5-5-25](#)(a)(1) and [IC 6-2.5-5-21](#)(b)(1).

In its protest letter, Taxpayer argues that the "instruments provided to purchasers of [Taxpayer's] implant products qualify as exempt 'durable medical equipment' or 'other medical supplies and devices' . . . " and also that "the instruments are exempt to the extent that they are leased by [Taxpayer] to 'state licensed hospital[s] or other qualifying nonprofit organizations.'" As noted above, the Revenue Ruling addressed both of these issues.

In the Revenue Ruling requested by Taxpayer, the Department cited to [45 IAC 2.2-5-36](#) in finding the surgical instruments were subject to the state's tax:

- (a) The gross retail tax shall apply to the following purchase transactions made by licensed practitioners:
 - (1) All office furniture, equipment and supplies.
 - (2) Drugs of a type not requiring a prescription, when not purchased for resale.
 - (3) *Surgical instruments, equipment and supplies.*
 - (4) *Bandages, splints, and all other medical supplies consumed in professional use.*
 - (5) *X-Ray, diathermy, diagnostic equipment, or any other apparatus used in the practice of surgery or medicine.*
- (b) The purchase of items for resale by the physician or surgeon. In order to resell items the practitioner must

be licensed as a retail merchant, and must quote the selling price of any items separately from the charge for professional service. (*Emphasis added*).

Taxpayer's Revenue Ruling stated:

On its face, the Department's regulation clearly states that the medical equipment, devices and supplies consumed in professional use are subject to Indiana sales tax. On its face, [IC 6-2.5-5-18\(a\)](#) clearly states that the exemption provided by that statutory provision relates only to sales of certain medical equipment, devices and supplies prescribed by someone licensed to issue a prescription. Since a prescription is issued and applies only to the patient to whom it has been written, the only reasonable interpretation of the statute read in conjunction with the regulation is that sales of exempt items to the holder of the prescription (i.e., the patient) are the only sales covered by the exemption. Since the transactions between Taxpayer and its customers (i.e., hospitals and surgical facilities) do not constitute sales to the patient, and do not represent sales prescribed by a person licensed to issue such a prescription, the transactions are not exempt under [IC 6-2.5-5-18\(a\)](#), regardless of whether the items sold qualify as durable medical equipment or other medical supplies and devices.

Also of importance is [45 IAC 2.2-5-27\(b\)](#), which states:

(a) The term "person licensed to issue a prescription" shall include only those persons licensed or registered to fit and/or dispense such devices.

(b) Definition: The term "prescribed" shall mean the issuance by a person described in paragraph 1 of this regulation [subsection (a) of this section] of a certification in writing that *the use of the medical equipment supplies and devices is necessary to the purchaser in order to correct or to alleviate a condition brought about by injury to, malfunction of, or removal of a portion of the purchaser's body.* (*Emphasis added*).

The regulation plainly states that, in order to qualify for the exemption, "the use of the medical equipment supplies and devices is necessary to the purchaser in order to correct or to alleviate a condition brought about by injury to, malfunction of, or removal of a portion of the *purchaser's body*." Taxpayer describes its customers as "state-licensed hospitals and other nonprofit healthcare institutions." [45 IAC 2.2-5-27\(b\)](#) makes it clear that it is the patient ("purchaser's body") that must be the purchaser for purposes of "prescribed," and in Taxpayer's case the patient is not purchasing the "specialized instruments." Taxpayer's protest on the "prescription" issue is denied.

Alternatively, Taxpayer argues that the surgical instruments are "leased" to "state licensed hospitals and other nonprofit healthcare organizations." As such, Taxpayer argues that the surgical instruments are exempt under IC § 6-2.5-4-10(a) and [45 IAC 2.2-4-27\(a\)](#).

IC § 6-2.5-4-10(a) provides that "[a] person, other than a public utility, is a retail merchant making a retail transaction when he rents or leases tangible personal property to another person other than for subrent or sublease."

[45 IAC 2.2-4-27\(a\)](#) provides that "[i]n general, the gross receipts from renting or leasing tangible personal property are taxable. This regulation [[45 IAC 2.2](#)] only exempts from tax those transactions which would have been exempt in an equivalent sales transaction."

Taxpayer argues that it receives "cash in exchange" for the instruments because the cost of these instruments is "embedded into the selling price of the [its] artificial hips, knees, and shoulders" Taxpayer further explains that it provides the instruments to hospitals and surgical facilities who "receive possession of the instruments and are responsible for losses from their damage or destruction." As such, the "shifting of financial responsibility for these highly valuable instruments plainly constitutes consideration."

Taxpayer has provided no evidence that it receives consideration from the hospitals and surgical facilities to whom it loans the instruments or that these medical facilities are bound by an undocumented "shifting of financial responsibility" if the instruments are lost or damaged. Taxpayer's argument that it is in the business of renting or leasing surgical instruments is inexact, undocumented, and entirely speculative. Taxpayer is reminded that the rule in Indiana is that "where such an exemption is claimed, the party claiming the same must show a case, by sufficient evidence, which is clearly within the exact letter of the law." *RCA Corp.*, 310 N.E.2d at 100-01. Taxpayer has failed to provide the requisite "sufficient evidence."

FINDING

Taxpayer's protest is respectfully denied.

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